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IN THE

Supreme Court of the United States

OCTOBER TERM, 1998

PENSION BENEFIT GUARANTY CORP.,

Petitioner,

v.

REORGANIZED CF&I FABRICATORS OF UTAH, INC., *et al.*

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

BRIEF IN OPPOSITION FOR RESPONDENTS REORGANIZED CF&I FABRICATORS OF UTAH, INC., *et al.*

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QUESTIONS PRESENTED

I. Whether the courts below correctly ruled that the bankruptcy claims of the Pension Benefit Guaranty Corporation ("PBGC") are pre-petition claims in bankruptcy, and therefore are not entitled to administrative priority in bankruptcy under 11 U.S.C. § 503(b) because the consideration for such claims was the pre-petition labor of the pension plan participants, and thus administrative priority does not apply.

II. Whether the courts below correctly ruled that in determining the amount of claims for future pension benefits "as of the date of the filing of the petition," under 11 U.S.C. § 502(b), they are not required to accept PBGC's present-value calculation, using different present-value assumptions developed for use solely under ERISA, without regard to bankruptcy law.

RULE 14.1(b) STATEMENT OF PARTIES TO THE PROCEEDING

The petition accurately lists the parties to the proceeding, with the following correction:

On November 7, 1990, the petition date of the underlying bankruptcy cases, CF&I Steel Corporation was publicly held and owned all of the stock of its nine subsidiaries: CF&I Fabricators of Utah, Inc., Colorado & Utah Land Company, Kansas Metals Company, Albuquerque Metals Company, Pueblo Metals Company, Denver Metals Company, Pueblo Railroad Service Company, CF&I Fabricators of Colorado, Inc., and Colorado and Wyoming Railway Company. These entities were the "Debtors" in the proceedings below.

On March 3, 1993, the effective date of the confirmed Chapter 11 plan in these cases, all stockholder interests were canceled, including the interests of CF&I Steel Corporation as sole stockholder of the other debtors. On and after March 3, 1993, the Debtors have been referred to as the "Reorganized Debtors." The Reorganized Debtors are now ten separate corporate shells without shareholders, elected officers, or directors. Each Reorganized Debtor is managed by Scott C. King, a representative of creditors under governance provisions approved by the Bankruptcy Court. Under the asset purchase agreement approved with the Chapter 11 plan, some of the names of the Reorganized Debtors were changed. The Reorganized Debtors' current names are: Reorganized CF&I Fabricators of Utah, Inc., Colorado & Utah Land Company, Kansas Metals Company, Albuquerque Metals Company, Reorganized Pueblo Metals Company, Denver Metals Company, Reorganized Pueblo

Railroad Service Company, Reorganized CF&I Fabricators of Colorado, Inc., Reorganized CF&I Steel Corporation, and The Reorganized Colorado & Wyoming Railway Company.

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STATUTES INVOLVED

The statutes involved are 11 U.S.C. §§ 502, 503, 507, 1113, 1114, 1123, and 29 U.S.C. §§ 1082, 1144, 1301, 1362.[2]

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1. This brief will use the following abbreviations in its citation of documents: "Pet." = Petition for a Writ of Certiorari; "Pet. App." = Appendix to Petition for a Writ of Certiorari; "Resp. App." = Appendix to Respondents Reorganized CF&I Fabricators of Utah, Inc., *et al.*, Brief in Opposition.

2. Citations to the United States Code are to the 1994 Edition, except that, if an earlier edition contained a different provision applicable in this case, the earlier edition's provision will be identified. Citations to the Code of Federal Regulations are to the 1998 Edition of Title XL, except that, if an earlier edition contained a different provision pertinent to this case, the earlier edition's provision will be identified.

STATEMENT OF THE CASE

A. Reorganized Debtors' Statement of the Case

The Reorganized Debtors are ten bankrupt corporations liquidating their assets for the benefit of creditors under a confirmed bankruptcy plan of reorganization (the "Plan of Reorganization") pursuant to Chapter 11 of the Bankruptcy Code, 11 U.S.C. §§ 101 *et seq*. PBGC is one of the largest unsecured creditors. Under the Plan of Reorganization, proceeds of the liquidation have been and will be distributed to creditors under the direction of a representative of creditors appointed by the Bankruptcy Court. Because the Reorganized Debtors are deeply insolvent, general unsecured creditors, who suffered hundreds of millions of dollars in actual pecuniary losses, will receive less than ten percent of their claims. Stockholders interests were abolished, and shareholders will receive nothing.

The Reorganized Debtors' predecessors, CF&I Steel Corporation ("CF&I") and its former subsidiaries (collectively, the "Debtors"), operated a steel plant and related businesses. CF&I sponsored two qualified pension plans for the Debtors' employees and retirees (the "Pension Plans") and was required by ERISA to meet minimum funding standards. Because of large losses in its steel business and a general decline in the steel industry, CF&I did not have sufficient revenues to pay its 1989 minimum funding payment of approximately $12.4 million which came due on September 15, 1990, resulting in the Debtors filing petitions under Chapter 11 of the Bankruptcy Code on November 7, 1990 (the "Petition Date"). Before and after the Petition Date, CF&I asked PBGC to terminate the larger of the Pension Plans (the "Master Plan"). PBGC denied CF&I's request until March 19, 1992, when PBGC terminated the Master Plan.

Only PBGC has power unilaterally to terminate pension plans. 29 U.S.C. § 1342(a) (ERISA § 4042(a)). Under 29 U.S.C. § 1341(a)(3) (ERISA § 4041(a)(3)), the Debtors could not unilaterally terminate the Master Plan because the Bankruptcy Code (11 U.S.C. § 1113(f)) prohibited the Debtors from any unilateral termination or alteration of its collective bargaining agreement with the United Steelworkers of America AFL-CIO-CLC ("USWA"), which required maintenance of the Pension Plans.

Because funding payments for retirees' pensions earned before the Petition Date are prepetition debts, the Debtors by law could not pay them after filing bankruptcy, 11 U.S.C. § 362, except under a confirmed plan of reorganization. *PBGC v. LTV Corp.*, 875 F.2d 1008, 1019 (2d Cir. 1989), *rev'd on other grounds*, 496 U.S. 633 (1990). Therefore, after the Petition Date, the Debtors could not correct the 1989 funding deficiencies or make any further prepetition pension funding payments except under a confirmed plan of reorganization. Debtors continued to pay prepetition retiree *health* benefits after the Petition Date required by the Bankruptcy Code. 11 U.S.C. § 1114(e). PBGC incorrectly implies that Debtors did something wrong by obeying these requirements of bankruptcy law. Pet. 6-7.

PBGC filed two substantially identical claims against each of the Debtors as to the terminated Master Plan. First, PBGC claimed $64,874,511 for alleged unpaid contributions to the Master Plan ("Minimum Contribution Claims") on many theories of priority, all but one of which, administrative priority under 11 U.S.C. § 503(b)(1)(A), PBGC has abandoned. Second, PBGC asserted a priority claim of $263,200,000 for an alleged insufficiency in assets of the Master Plan to pay pensions ("Unfunded Benefits Claim"). Pet. App. 4a, 82a.

PBGC now asserts no priority for its Unfunded Benefits Claim after it was denied below but asserts a general unsecured claim. Pet. App. 4a-5a, 48a-49a.

PBGC was granted an administrative claim for the postpetition "normal cost" component of its pension claims (that portion attributable to postpetition services of employees). Pet. App. 12a n.5. PBGC was also granted a prepetition priority claim under 11 U.S.C. § 507(a)(4) (limited unsecured prepetition claims for contributions to employee benefit plans) for a portion of its claim that is not in dispute here. PBGC's allowed administrative and priority claims (approximately $2 million) were paid in full, pursuant to the confirmed Chapter 11 plan. Under the Plan of Reorganization PBGC received a valuable partnership interest in the new owner of the steel plant and will receive other distributions on par with other unsecured creditors.

PBGC scoldingly asserts that "as a result of Respondents' failure to fund their Pension Plan and the agency's obligation to pay guaranteed benefits, PBGC sustained a loss of nearly a quarter billion dollars." Pet. 3.

What really occurred, however, is this: (i) as a result of Debtors' inability (not "failure") to have enough cash to contribute to the Master Plan, the Debtors filed for relief under Chapter 11; (ii) as a result of the Chapter 11 filing, Debtors could not contribute to the Master Plan; (iii) as a result of the inability (not "failure") of Debtors to fund the Master Plan, PBGC after a long delay terminated the Master Plan; and (iv) as a result of PBGC's statutory mission (not Debtors' "failure"), PBGC has paid guaranteed pension benefits in accordance with law. That is PBGC's statutory duty. Before PBGC may validly claim "losses," PBGC must deduct its premium, investment,

and other income, including PBGC's recoveries in this case, the same as any insurer would do.

PBGC operates on private, not government, funds — premiums from plan sponsors and assets from terminated plans. PBGC Br. 6. Guaranteed pension benefits are not paid from collection of taxes or out of general federal revenues. Pet. 4.

Among the remaining creditors is a trust to provide medical benefits to the retirees of the defunct companies, and the PBGC. Priority payments, or increased payments, to the PBGC will reduce, therefore, the amounts to be received by the other creditors, including the same retirees who are recipients of guaranteed and non-guaranteed pension benefits from the PBGC, whom that agency is statutorily empowered to protect. In that sense, PBGC is in a conflict with the members of its own protected class.

B. Identification, Under Rule 15.2, of PBGC's Mis-Statements of the Case

In some respects, PBGC's "Statement of the Case" (Pet. 2) is less than accurate and far from fair. [3] PBGC's Statement

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3. PBGC's opening assertion that "PBGC sustained a loss of nearly a quarter billion dollars" seeks to expand the magnitude of the agency's stake in the issues presented *here* far beyond the adjudicated reality. PBGC's failure to sustain its bloated original set of claims was the result of losing issues for which it has not sought further review. PBGC had asserted a claim for a "lien" arising upon termination of the CF&I pension plan, and the courts below denied that claim because the automatic stay nullified the purported lien. Pet. App. 48a-49a, 94a-95a. PBGC's Statement of the Case continues to describe a "lien" for delinquent contributions (Pet. 4), although the courts below barred that lien claim because the date of its purported occurrence — 60 days after the amount of the delinquency exceeded $1 million — was postpetition and therefore barred by the automatic stay, 11 U.S.C. § 362. Pet. App. 5a-9a, 44a-46a, 95a.

of the Case includes a lengthy outside-the-record description of how the agency's plan termination insurance program is operated (Pet. 3-6), including selected references to portions of one statute (ERISA, the Employee Retirement Income Security Act of 1974), without reference to the Bankruptcy Code, the primary statute governing this case.

The notion that PBGC has "sustained a loss of nearly a quarter billion dollars" (Pet. 3) ignores the fact that PBGC, like every insurer, is in the business of paying insured benefits, and that the insurer's payment of benefits does not cause a "loss" in the long run if the benefits are offset by premium and other income in the long run. In fact, PBGC's latest annual report, issued only last month, shows a very handsome net income of $1.531 billion in its single-employer insurance program, and total return on investments of 14.4%, with investment income exceeding actuarial charges.[4] PBGC's Statement of the Case also seeks to balance its financial exposure in this case against a stipulated limitation on PBGC's recovery from the "Appeal Funds" set aside in CF&I confirmed plan of reorganization (Pet. 7). That limitation, however, is not evidence that only PBGC has a stake in the outcome here. On the contrary, the "Appeal Funds" were stipulated as part of the negotiated plan of reorganization (Pet. App. 4a) precisely because PBGC's legal position — a position for which PBGC seeks to establish a precedent here — would have given the PBGC the right to overwhelm the claims of all other unsecured creditors.

In its "Statement of the Case," PBGC insists that Congress expressly gave the agency the right to set its own discount rate (Pet. 5-6) for both ERISA and bankruptcy cases (Pet. 14). The statement is incorrect on the law; but right or wrong, the

4. PBGC 1998 Ann. Rep. 23, Resp. App. 15a-17a.

particulars of this case are peculiarly inappropriate for current review. The previous agency regulations relied upon by the PBGC (and lodged with the Court by them) have been superseded and re-superseded. Only a year after their issuance PBGC modified them for the express reason that the interest rate used in those old regulations and relied upon by PBGC at that time was out-of-line with annuity market rates. 58 Fed. Reg. 50,812 (1993) (to be codified at 29 C.F.R. pts. 2619 and 2676) (discussed under Point II, *infra*).

PBGC states that rulings below are an "inducement for solvent companies to enter bankruptcy." (Pet. 15). The argument is simply at odds with the factual evidence in the case, including the facts that

> CF&I met its funding obligations until a decline in economic conditions of the American steel industry left it unable to make minimum funding contributions of approximately $14 million. This state of affairs led CF&I into filing a Petition for Relief under chapter 11 of the Bankruptcy Code.

(Pet. App. 3a). The adjudicated facts of this case are controlling here, and among those facts is the finding that CF&I was not a solvent company when it filed Chapter 11, and was in bankruptcy precisely because it was financially unable (not unwilling) to make further contributions to its pension plan.

On the discount rate issue, PBGC asserts that the court of appeals' decision "means that the agency's regulation no longer serves as a uniform benchmark of a plan's benefit liabilities in all circumstances." (Pet. 16). The notion that PBGC's wish for a "uniform benchmark" should override the bankruptcy court's statutory duty to treat all unsecured creditors equally by applying a uniform discount rate for creditors of a particular debtor is an apples-and-oranges distortion, injecting a non-

germane agency bookkeeping concern into the statutory duty of a bankruptcy court under 11 U.S.C. § 502(b) to "determine the amount of such claim . . . as of the date of the filing of the petition" — that is, to provide equal treatment among creditors of a specific debtor.[5]

The PBGC clearly knows how to lobby for its objectives legislatively, having legislatively enhanced its position in 1986 and 1987.[6] Indeed, PBGC has tried to accomplish an advancement of its priorities in bankruptcy legislatively, but

5. Pet. App. 22a. To illustrate, assume Creditor A is entitled to a future stream of payments of $1 million per year for ten years, and Creditor B is entitled to $10 million on the petition date. If Creditor A's claim were discounted using an artificially low discount rate, Creditor A would receive a substantial amount of unmatured interest. Assuming a market discount rate of 12.3% and that the rate sought by Creditor A were 6.5%, the net present value ("NPV") of Creditor A's ten-year payment stream would be as follows:

NPV @ 12.3% rate = $5,581,507 NPV @ 6.5% rate = $7,188,830

If the net present value amount using the 12.3% market rate ($5,581,507) were invested in the market and earned 12.3% interest, the future value of that present value amount would be $10,000,000. If the net present value amount using the 6.5% rate ($7,188,830) earned the market rate of 12.3% interest, the future value of this present value amount would be $12,879,730. By the end of ten years, Creditor A would have received nearly $2.9 million in investment earnings in addition to its ten $1 million payments. Distributions to Creditors A and B would not be equal due to the deflated rate used to value Creditor A's claim. To treat both creditors equitably, Creditor A's claim must be discounted to present value using a discount rate which reflects the future earning power of Creditor A's claims distribution.

6. Single-Employer Pension Plan Amendments Act of 1986, Title XI of the Consolidated Omnibus Budget Reconciliation Act of 1986, (Cont'd)

failed.[7] PBGC's unsuccessful quest for legislation granting the priorities it asks this Court to create for it is noted in Giddens, "Attempting to Protect Employee Retirement Income Within Bankruptcy Reorganization: PBGC Efforts to Obtain Priority Status," 1993 Ann. Rev. Banking L. 397, 423-24 (1993); Dennis R. Dow and Mark Moedritzer, *ERISA-Related Claims in Bankruptcy*, 3 J. BANKR. L. & PRAC. 76, 94 (1993); and *In re Kent Plastics Corp.*, 183 B.R. 841, 845-46 (Bankr. S.D. Ind. 1995).

PBGC's purported purpose in urging its unrealistic discount rate ("uniform benchmark") obscures, moreover, the agency's real purpose in setting that rate. This admitted purpose is to act as a deterrent to an employer who might be tempted to voluntarily foist pension liabilities upon the agency, even though the employer could well afford to fund them. That "institutional goal" was a factual finding of the district court, based on admissions of the PBGC,[8] but it is not the purpose or provision of the Bankruptcy Code.

(Cont'd)
Pub. L. No. 99-272, 100 Stat. 82 (1986); Pension Protection Act of 1987, included in the Omnibus Budget Reconciliation Act of 1987, Pub. L. No. 100-203, 101 Stat. 1330 (1987). Despite PBGC efforts, neither bill advanced PBGC's claims in bankruptcy.

7. See S. 1730, 99th Cong. § 996, at 578-79 (as reported, October 2, 1985), which would have amended ERISA Title IV to give PBGC a tax priority for a "lien" under Title IV and provided that "[t]he lien and perfection of the lien shall be treated as fixing a statutory lien that is not avoidable under section 545 of title 11, United States Code." After this and other priority language of S. 1730 was incorporated in the Consolidated Omnibus Budget Reconciliation Act, the final language of that bill (H.R. 3128, 99th Cong. (1986)) gave no such priority. See H.R. Conf. Rep. No. 99-453, at 576 (1985).

8. Pet. App. 36a: "PBGC's own institutional goal of making plan terminations less attractive than the purchase of close-out annuities."

REASONS FOR DENYING THE WRIT

There are no compelling reasons to grant certiorari, and there are strong reasons not to do so. This bankruptcy case involves no constitutional question, no conflict with this Court's decisions, no conflict among the circuits, no dissenting opinion below, and not even a single judge wishing to hear reconsideration en banc. The Tenth Circuit ruling is consistent with those in other circuits. The particular PBGC valuation methodology which the PBGC seeks tc inject into valuation proceedings of the bankruptcy court is in fact a methodology which the PBGC has already abandoned because of its acknowledged "disparity between the PBGC's low interest rates and familiar private sector rates." 58 Fed. Reg. 50,812 (September 28, 1993). And the Tenth Circuit's rulings rejecting administrative priority and insisting on use of the court's own present-value claims evaluation are plainly consistent with the provisions of the Bankruptcy Code governing Chapter 11 proceedings.

I.

THERE IS NO COMPELLING REASON TO GRANT THE WRIT: THE TENTH CIRCUIT'S DECISION PRESENTS NO CONSTITUTIONAL CONFLICT, NO CONFLICT WITH ANY DECISION OF THIS COURT, NO CONFLICT AMONG THE CIRCUITS, NO DISSENT BELOW, AND IS CONSISTENT WITH THE DECISIONS IN OTHER CIRCUITS

While PBGC argues that there are important issues raised in this bankruptcy case, this is not an appropriate case in which to address them, and there are no "compelling reasons" warranting the grant of certiorari. Sup. Ct. R. 10.

The petition cites no conflict among the courts of appeals (Sup. Ct. R. 10(a)). PBGC'S Petition acknowledges the consistent rulings in three cases that have considered the discount rate issue. Pet. 14 n.10.[9] Likewise, on the claim of PBGC's administrative priority in bankruptcy, the petition claims no conflict in circuits, and acknowledges consistent rulings in the circuits that have considered the question. (Pet. 27).

There was not even a dissent in the Court of Appeals for the Tenth Circuit, and on motion for reconsideration not a single judge of the Court of Appeals supported reconsideration en banc. Indeed, the only time the PBGC ever persuaded even a dissenting judge on either of these issues was in *PBGC v. Sunarhauserman, Inc. (In re Sunarhauserman, Inc.)*, 126 F.3d 811, 822 (6th Cir. 1997) (dissenting opinion), but on a motion for reconsideration in that case, once again not a single other judge of that Court of Appeals supported reconsideration en banc. *PBGC v. Sunarhauserman, Inc. (In re Sunarhauserman, Inc.)*, 1997 U.S. App. LEXIS 37157 (6th Cir. Dec. 8, 1997). And PBGC did not petition for certiorari in that case.

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9. Citing *LTV Corp. v. PBGC (In re Chateaugay Corp.)*, 130 B.R. 690, 695-96 (S.D.N.Y. 1991), and 126 B.R. 165 (Bankr. S.D.N.Y. 1991), *vacated by consent order*, 17 Empl. Ben. Cas. (BNA) 1102 (S.D.N.Y. 1993); *Belfance v. PBGC (In re CSC Industries, Inc.)*, No. 95-4103 (Bankr. N.D. Ohio Dec. 3, 1997), *appeal docketed*, No. 4:99CV00041 (N.D. Ohio, Jan 8, 1999).

II.

THE PBGC REGULATIONS AT ISSUE HERE HAVE BEEN SUPERSEDED, AND RE-SUPERSEDED AND PRESENT ONLY AN OBSOLETE CONTEXT FOR CONSIDERATION OF THE VALUATION ISSUE

The obsolete regulatory context in which this case arises makes it particularly inappropriate for further review by certiorari. The 1992 version of PBGC's valuation regulation, which PBGC lodged with the Court, was supplanted a year later. While PBGC insists that the 1993 amended regulation was "without change to its basic approach" (Pet. 6 n.5), in fact the preamble to the 1993 regulations conceded that a reason for the change was the prior regulation's "disparity between the PBGC's low interest rates and familiar private sector rates." 58 Fed. Reg. 50,812 (September 28, 1993), Resp. App. 20a.[10] The 1993 superseding regulation claims to adhere to PBGC's stated commitment to "accurately reflect private sector group *annuity prices*" (*Id.* 20a) (emphasis added), but concedes that it in fact involved a "disparity between PBGC's low *interest rates* and familiar private sector *rates*." (*Id.*). Doubtless PBGC has an adequate explanation to support its notion that "for most plans, this amendment will not significantly affect the valuations produced" (Resp. App. 18a), and in any event the private sector *insurance rates* urged by PBGC are not market rates of interest at all, in the bankruptcy sense. Be that as it may, the context in which the interest rate issue is presented by PBGC's petition in this case is simply the wrong context for certiorari. The specific regulation which the PBGC asks this Court to impose upon a bankruptcy court's market

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10. The 1993 regulation was re-superseded, in turn, by the current regulation, which was promulgated in 1996. 29 C.F.R. § 4044.52, 61 Fed. Reg. 34002 (1996).

valuation under 11 U.S.C. § 502(b), is not merely obsolete, it was admittedly wrong. It presents, therefore, the wrong context in which to test the currently-effective PBGC valuation regulation. This context does not invoke a "compelling reason" for the grant of certiorari.

III.

THE REMAINING ISSUES IN THIS CASE LACK THE CONTEXT NECESSARY TO EVALUATE THE IMPACT ON THE "AGENCY'S ABILITY TO CARRY OUT ITS MISSION"

PBGC argues that its petition should now be granted because "immediate review of these issues is important to the agency's ability to carry out its mission." Pet. 19. PBGC carries out its mission, however, by filing a much wider array of claims in each bankruptcy. That is what PBGC did in this case. PBGC litigated all those claims in the Bankruptcy Court and District Court. It dropped some of them in the Court of Appeals (although the major issue it dropped was in fact tenaciously argued at the same time in another case),[11] and it has dropped more issues in its petition here. Pet. 10 n.7. Thus, the case presented here does not give the Court an adequate or accurate picture of the PBGC's ongoing litigation posture in seeking "to carry out its mission."

PBGC insists that "the 'world of bankruptcy' — to which the court of appeals ostensibly limited its holding — is the main world in which the PBGC insurance fund operates." Petit. 14. That argument is both immaterial and wrong. The statute, of course, was designed in 1974 and originally provided that a

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11. *PBGC v. Skeen (In re Bayly Corp.)*, 163 F.3d 1205 (10th Cir. 1998).

plan termination required no bankruptcy, nor even economic distress. Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, § 4041(a), 88 Stat. 829, 1020 (1974). While later amendments injected, and current law includes, voluntary termination requirements of economic "distress," ERISA § 4041, 29 U.S.C. § 1341, not all of those requirements include proceedings in Bankruptcy. ERISA § 4041(c)(2)(B)(iii), 29 U.S.C. § 1341(c)(2)(B)(ii).

Even more to the point, *this* case does not involve a voluntary plan termination. On the contrary, this was an involuntary plan termination, initiated by the PBGC under ERISA § 4042, 29 U.S.C. § 1342. Involuntary terminations may be initiated at any time the PBGC believes that its financial exposure would "increase unreasonably." Indeed, PBGC's legal strategy is the use of its "early warning system," in which PBGC learns of an impending corporate transaction (spin-off, sale of assets, etc.), and induces the economically healthy plan sponsor to make an extra contribution to the sponsor's pension plan by threatening the sponsor with an involuntary plan termination under ERISA § 4042, leading to a lien for the full amount of unfunded liabilities — outside of any bankruptcy and therefore immune from any stay or other restriction of the Bankruptcy Code. The 1998 Annual Report of PBGC, under the heading "Loss Prevention," describes this system as being "PBGC's principal performance measure for its strategic goal of protecting existing defined benefit plans and their participants . . ." PBGC 1998 Ann. Rep. 14, Resp. App. 14a. Clearly, the PBGC's non-bankruptcy enforcement rights are not only alive and well, but also the central component of PBGC's overall corporate strategy.

IV.

THE TENTH CIRCUIT CORRECTLY DENIED ADMINISTRATIVE PRIORITY

The Tenth Circuit's refusal to grant administrative priority was for unfunded benefit liabilities of the Master Plan correct.

A. Claims for Unfunded Pension Liabilities or for Contributions to Fund Such Pension Benefits are Prepetition Debts Because the Pensions Were Earned by Prepetition Service

All of PBGC's remaining claims arise from pension benefits earned under the Master Plan by work performed before CF&I filed its bankruptcy petition.

PBGC's allowed postpetition administrative claim, for minor amounts of pension benefits earned by postpetition labor, has already been paid in full pursuant to the confirmed Chapter 11 plan of reorganization.

PBGC also claimed and was granted a prepetition priority claim under 11 U.S.C. § 507(a)(4) (limited unsecured prepetition claims for contributions to employee benefit plans) for a portion of its claim that is not in dispute here. That claim was paid pursuant to the confirmed plan of reorganization. That claim, however, clearly demonstrates that the Bankruptcy Code itself treats pensions, and pension funding obligations, as prepetition debts if the work that earned the pensions was done prepetition. Section 507(a)(4) of the Bankruptcy Code grants this priority to "unsecured claims for contributions to an employee benefit plan . . . arising from services rendered within 180 days before the date of the filing of the petition. . . ." The Bankruptcy Code's specific treatment of plan benefits as

"arising from services rendered . . . before the date of the filing of the petition" is definitive of the prepetition character of the funding claim.

PBGC's remaining claims are not attributable to postpetition services of the Debtors' employees. Their character as prepetition claims is based on undisputed facts found by the lower courts. Pet. App. 89a-91a.

When PBGC chose to terminate unilaterally the Master Plan and become the successor trustee, it succeeded to the Master Plan's prepetition claims against the Debtors. The mere postpetition change of the trustee of the Master Plan from CF&I to PBGC (or the postpetition transfer of the Master Plan's prepetition claims to PBGC) does not convert prepetition claims into post-petition claims any more than does a postpetition change in management of a creditor or the postpetition assignment of a prepetition claim.

The great weight of authority holds that liabilities are not "incurred" postpetition simply because they become due post-petition. *PBGC v. Sunarhauserman, Inc. (In re Sunarhauserman, Inc.)*, 126 F.3d 811, 816-819 (6th Cir. 1997) (rejecting PBGC's attempts to obtain postpetition status for prepetition claims); *Trustees of Amalgamated Ins. Fund v. McFarlin's, Inc.*, 789 F.2d 98, 101 (2d Cir. 1986); *Coldwell Banker & Co. v. Godwin Bevers Co. (In re Godwin Bevers Co.)*, 575 F.2d 805, 807 (10th Cir. 1978) (prepetition commission agreement did not give rise to administrative claim under Bankruptcy Act when property was sold postpetition); *Cramer v. Mammoth Mart, Inc. (In re Mammoth Mart, Inc.)*, 536 F.2d 950, 954 (1st Cir. 1976) ("a claimant who fully performs under a contract prior to the filing of the petition will not be entitled to first priority even though his services

may have resulted in a direct benefit to the bankrupt estate after the filing"); *Gallivan v. Springfield Post Road Corp.*, 110 F.3d 848 (1st Cir. 1997) (same result under Bankruptcy Code, applying *Mammoth Mart* analysis); *In re Great N.E. Lumber & Millwork Corp.*, 64 B.R. 426 (Bankr. E.D. Pa. 1986); *In re Johns-Manville Corp.*, 57 B.R. 680, 690 (Bankr. S.D.N.Y. 1986) (appropriate focus for determining when a claim arises is "the time when the acts giving rise to the alleged liability were performed").

As Judge Lifland correctly analyzed this issue in the landmark *LTV* cases:

> The PBGC's right to payment upon termination was, on the petition date, a classic prepetition contingent claim. The postpetition termination of the pension plans did not transform the PBGC's contingent pre-petition claims into post-petition claims.

LTV Corp. v. PBGC (In re Chateaugay Corp.), 115 B.R. 760, 775 (Bankr. S.D.N.Y. 1990),[12] reiterated in *In re Finley, Kumble, Wagner, Heine, Underberg, Manley, Myerson & Casey*, 160 B.R. 882 (Bankr. S.D.N.Y. 1993). The district court in *LTV Corp. v. PBGC (In re Chateaugay Corp.)*, 130 B.R.

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12. On June 7, 1993, some of the *LTV* decisions were vacated by consent of the parties, including *LTV Corp. v. PBGC (In re Chateaugay Corp.)*, 115 B.R. 760 (Bankr. S.D.N.Y. 1990), *LTV Corp. v. PBGC (In re Chateaugay Corp.)*, 126 B.R. 165 (Bankr. S.D.N.Y. 1991), and *LTV Corp. v. PBGC (In re Chateaugay Corp.)*, 130 B.R. 690 (S.D.N.Y. 1991). Vacatur does not deprive these decisions of their persuasive value and this Court is free to adopt their highly persuasive reasoning. *See In re Finley, Kumble, Wagner, Heine, Underberg, Manley, Myerson & Casey*, 160 B.R. 882, 898 (Bankr. S.D.N.Y. 1993).

690, 697 (S.D.N.Y. 1991), agreed: "PBGC's claims are pre-petition contingent claims because the labor giving rise to the pension obligations was performed pre-petition."

In treating PBGC's claims as prepetition claims, the Tenth Circuit was squarely in line with the foregoing well established precedent.

B. *Reading Co. v. Brown* Does Not Require a Different Result

The keystone of PBGC's argument for first priority is the Petition's reliance on *Reading Co. v. Brown*, 391 U.S. 471 (1968). Pet. 26. *Reading*, however, involved a debt that was *incurred postpetition*. As the Petition itself recites, "the Court granted administrative priority to a postpetition tort claim" because the claimant's "property was damaged by a fire through the negligence of the receiver." In each of the later cases following *Reading*, cited by PBGC (Pet. 26-27),[13] the debtor's conduct which gave rise to the claim occurred

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13. *Cumberland Farms Inc. v. Florida Dep't of Envtl. Protection*, 116 F.3d 16, 20-21 (1st Cir. 1997) (postpetition operation of underground storage tanks without satisfying financial responsibility requirements); *Alabama Surface Mining Comm'n v. N.P. Mining Co. (In re N.P. Mining Co.)*, 963 F.2d 1449, 1453-58 (11th Cir. 1992) (postpetition environmental violations); *United States v. LTV Corp., (In re Chateauguay Corp.)*, 944 F.2d 997, 1009-10 (2d Cir. 1991) (response costs of postpetition maintenance of hazardous waste sites); *Lancaster v. Tennessee (In re Wall Tube & Metal Prods. Co.)*, 831 F.2d 118, 123-24 (6th Cir. 1987) (response costs as to hazardous wastes still on Debtor's land postpetition); *Spunt v. Charlesbank Laundry, Inc. (In re Charlesbank Laundry, Inc.)*, 755 F.2d 200, 203 (1st Cir. 1985) (postpetition continuation of nuisance); *Yorke v. NLRB*, 709 F.2d 1138, 1143 (7th Cir. 1983) (back pay order against Trustee in bankruptcy who violated NLRA postpetition).

postpetition. In CF&I's case, the pension debt was incurred by the prepetition labor of CF&I's employees. *Reading* and its progeny are not in point.

PBGC is even farther off the mark when the petition (Pet. 28) argues that "[t]he employer's statutory obligation to pay contributions to the plan is entirely separate from the plan's obligation to participants," citing *Hughes Aircraft Co. v. Jacobson*, 119 S. Ct. 755, 762 (1999). The Court's *Hughes* ruling had nothing to do with bankruptcy, and had nothing to do with the question whether the obligation to fund was a postpetition or prepetition debt. *Hughes*, a fiduciary duty case under ERISA title I, simply held that the use of excess, overfunding, assets to benefit other participants did not violate ERISA's fiduciary standards.

V.

THE TENTH CIRCUIT CORRECTLY APPROVED THE BANKRUPTCY COURT'S MARKET VALUATION METHOD AS REQUIRED BY 11 U.S.C. § 502(b), RATHER THAN PBGC'S REGULATORY DISCOUNT RATE

The Tenth Circuit correctly upheld the bankruptcy court's decision on the discount rate applicable to bringing future pension payment obligations to present value.

The issue presented by the Petition is whether PBGC's original Unfunded Benefits Claim used the proper valuation method *in bankruptcy*. The parties do not dispute PBGC's calculation of the aggregate *future value* of its Unfunded Benefits Claim. The dispute lies in the methodology by which the *present value* of PBGC's claim should be determined.

The courts below properly ruled that PBGC's Unfunded Benefits Claim should be reduced to present value using a market-based discount rate of 12.3%, which fairly reflects the expected rate of return a prudent investor may achieve on the investment of a sum of money set aside as of the Petition Date to satisfy future benefit payments, and "is the only rate in evidence compatible with the Bankruptcy Code." Pet. App. 23a.

PBGC, on the other hand, asserts based on ERISA that it has the unilateral prerogative to establish the discount rate for its own claim and to impose that rate upon the bankruptcy court, to the detriment of other unsecured creditors. PBGC contends that its claim should be discounted utilizing a single-creditor-specific discount rate of 6.5% embodied in its own regulation, Pet. App. 21a. That is a rate PBGC devised to suit its own administrative convenience and to promote PBGC's own "institutional goal of making plan termination less attractive," Pet. App. 22a. Applying the ERISA discount factor to value PBGC's bankruptcy claim, however, would undermine the fundamental bankruptcy principle of equality of distribution among similarly situated creditors. 11 U.S.C. § 502(b)(2).

The courts below properly recognized the applicability of the fundamental bankruptcy principle of equality of treatment between similarly situated creditors to bankruptcy claims allowance. Pet. App. 13a-14a. Adherence to the principle of equal treatment is more essential where the claim to be valued is a claim for a future stream of payments. The Bankruptcy Code mandates that claims for future payments be discounted to present value. 11 U.S.C. § 502(b) ("the court . . . shall determine the amount of such claim in lawful currency of the United States as of the date of the filing of the petition . . ."). The regulatory interest rate assumption proffered by the PBGC

applies to the present-valuing of future benefits under a different statute (ERISA), in a different context, and for a different purpose (to discourage plan terminations).[14]

As the *LTV* bankruptcy court recognized, "based on its charter, the PBGC is clearly motivated to enhance its claims . . . as much as possible." *LTV Corp. v. PBGC (In re Chateaugay Corp.)*, 115 B.R. 760, 771 (Bankr. S.D.N.Y. 1990). Under the Bankruptcy Code, the court, not the creditor, is charged with the responsibility to determine the present value of a claim for a future stream of payments. *Id.* at 765-71. Allowing PBGC to dictate an artificially low discount rate would enable PBGC to inflate the value of its own claim. Creditors, however, are not granted that privilege. PBGC's discount factor is fundamentally inconsistent with 11 U.S.C. §§ 502(b), 502(b)(2), 1123(a)(4) and the equitable bankruptcy principles inherent in those statutory provisions.

PBGC's position rests entirely upon its unsupportable contention that the Bankruptcy Code must be subordinated to PBGC's non-bankruptcy regulation. PBGC attempts to justify its untenable position by arguing that its regulation is entitled to absolute deference as "legislative rules," and that the non-bankruptcy law embodied in its regulation is the only law to be applied in determining the validity and amount of its Unfunded Benefits Claim. Pet. 21-22. PBGC relies heavily on its analysis of *Batterton v. Francis*, 432 U.S. 416 (1977), *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), and related cases. PBGC tries to show that its valuation regulation carries the force of law and thereby prevails over inconsistent provisions of the Bankruptcy Code.

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14. 29 C.F.R. § 2619.1 at 666 (7-1-92 Edition) (from Material Lodged in Support of Petition for Certiorari, at 1).

PBGC's reliance on *Batterton* and *Chevron* is misplaced. Moreover, even assuming *arguendo* that PBGC's 1992 regulation has the force and effect of law, its status as a legislative rule does not justify subordination of the Bankruptcy Code.

In *Batterton* and *Chevron*, the Supreme Court addressed the degree of deference to be accorded an administrative agency in the context of reviewing the agency's construction of the statute it administers. *Batterton*, 432 U.S. at 424; *Chevron*, 467 U.S. at 842. In that context, the Court ruled that where Congress has expressly authorized the agency to elucidate a specific provision of the statute by regulation, the agency's construction is to be given "controlling weight" unless it is arbitrary, capricious, or manifestly contrary to law. *Chevron*, 467 U.S. at 844 (citing *Batterton*, 432 U.S. at 425). In reaching its decision, the Court recognized that an agency's construction of the statute *it administers* is an area in which it has special expertise, and because of that expertise, the agency is entitled to substantial deference.

The Court's rulings in *Batterton* and *Chevron* do not apply in the instant case, and the Court of Appeals correctly saw it that way. Pet. App. 14a-15a. This case does not present an issue concerning an administrative agency's construction of the statute which *it administers*.[15] PBGC administers ERISA, not the Bankruptcy Code. The Reorganized Debtors do not challenge the discount factor set forth in the 1992 PBGC

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15. Valuation of PBGC's claims requires the Bankruptcy Court to "reconcil[e] conflicting policies" between ERISA and the Bankruptcy Code, a task which PBGC is not at all authorized, or equipped, to perform. *LTV Corp. v. PBGC (In re Chateaugay Corp.)*, 115 B.R. 760, 768-71 (Bankr. S.D.N.Y. 1990); *cf. Chevron*, 467 U.S. at 844.

regulation as an improper construction of ERISA. The issue in this case is whether PBGC's discount factor should be applied, outside of ERISA, to value a claim in bankruptcy at present value.

Any delegation of legislative authority arguably expressed in 29 U.S.C. § 1301(a)(18) (ERISA § 4001(a)(18)) does not extend to the valuation of claims in bankruptcy. Section 1301(a)(18) defines the amount of unfunded benefit liabilities "for purposes of this title [ERISA]" only. Nothing in § 1301(a)(18), or any other provision of ERISA, expresses any congressional intent to authorize PBGC to determine the present value of unfunded future benefit liabilities for purposes of the Bankruptcy Code. Rather, Congress expressly delegated exclusive responsibility for valuation of all claims in bankruptcy, whatever their source, to the Bankruptcy Court in § 502(b).

CONCLUSION

The Court should deny the petition.

Respectfully submitted,

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APPENDIX

APPENDIX A — RELEVANT STATUTES

11 U.S.C. § 1113

Sec. 1113. Rejection of collective bargaining agreements

(a) The debtor in possession, or the trustee if one has been appointed under the provisions of this chapter, other than a trustee in a case covered by subchapter IV of this chapter and by title I of the Railway Labor Act, may assume or reject a collective bargaining agreement only in accordance with the provisions of this section.

(b)

> (1) Subsequent to filing a petition and prior to filing an application seeking rejection of a collective bargaining agreement, the debtor in possession or trustee (hereinafter in this section "trustee" shall include a debtor in possession), shall —
>
> > (A) make a proposal to the authorized representative of the employees covered by such agreement, based on the most complete and reliable information available at the time of such proposal, which provides for those necessary modifications in the employees benefits and protections that are necessary to permit the reorganization of the debtor and assures that all creditors, the debtor and all of the affected parties are treated fairly and equitably; and

(B) provide, subject to subsection (d)(3), the representative of the employees with such relevant information as is necessary to evaluate the proposal.

(2) During the period beginning on the date of the making of a proposal provided for in paragraph (1) and ending on the date of the hearing provided for in subsection (d)(1), the trustee shall meet, at reasonable times, with the authorized representative to confer in good faith in attempting to reach mutually satisfactory modifications of such agreement.

(c) The court shall approve an application for rejection of a collective bargaining agreement only if the court finds that —

(1) the trustee has, prior to the hearing, made a proposal that fulfills the requirements of subsection (b)(1);

(2) the authorized representative of the employees has refused to accept such proposal without good cause; and

(3) the balance of the equities clearly favors rejection of such agreement.

Appendix A

(d)

(1) Upon the filing of an application for rejection the court shall schedule a hearing to be held not later than fourteen days after the date of the filing of such application. All interested parties may appear and be heard at such hearing. Adequate notice shall be provided to such parties at least ten days before the date of such hearing. The court may extend the time for the commencement of such hearing for a period not exceeding seven days where the circumstances of the case, and the interests of justice require such extension, or for additional periods of time to which the trustee and representative agree.

(2) The court shall rule on such application for rejection within thirty days after the date of the commencement of the hearing. In the interests of justice, the court may extend such time for ruling for such additional period as the trustee and the employees' representative may agree to. If the court does not rule on such application within thirty days after the date of the commencement of the hearing, or within such additional time as the trustee and the employees' representative may agree to, the trustee may terminate or alter any provisions of the collective bargaining agreement pending the ruling of the court on such application.

(3) The court may enter such protective orders, consistent with the need of the authorized

representative of the employee to evaluate the trustee's proposal and the application for rejection, as may be necessary to prevent disclosure of information provided to such representative where such disclosure could compromise the position of the debtor with respect to its competitors in the industry in which it is engaged.

(e) If during a period when the collective bargaining agreement continues in effect, and if essential to the continuation of the debtor's business, or in order to avoid irreparable damage to the estate, the court, after notice and a hearing, may authorize the trustee to implement interim changes in the terms, conditions, wages, benefits, or work rules provided by a collective bargaining agreement. Any hearing under this paragraph shall be scheduled in accordance with the needs of the trustee. The implementation of such interim changes shall not render the application for rejection moot.

(f) No provision of this title shall be construed to permit a trustee to unilaterally terminate or alter any provisions of a collective bargaining agreement prior to compliance with the provisions of this section.

11 U.S.C. § 1114

Sec. 1114. Payment of insurance benefits to retired employees

(a) For purposes of this section, the term "retiree benefits" means payments to any entity or person for the purpose of

providing or reimbursing payments for retired employees and their spouses and dependents, for medical, surgical, or hospital care benefits, or benefits in the event of sickness, accident, disability, or death under any plan, fund, or program (through the purchase of insurance or otherwise) maintained or established in whole or in part by the debtor prior to filing a petition commencing a case under this title.

(b)

(1) For purposes of this section, the term "authorized representative" means the authorized representative designated pursuant to subsection (c) for persons receiving any retiree benefits covered by a collective bargaining agreement or subsection (d) in the case of persons receiving retiree benefits not covered by such an agreement.

(2) Committees of retired employees appointed by the court pursuant to this section shall have the same rights, powers, and duties as committees appointed under sections *1102* and 1103 of this title for the purpose of carrying out the purposes of sections *1114* and 1129(a)(13) and, as permitted by the court, shall have the power to enforce the rights of persons under this title as they relate to retiree benefits.

(c)

(1) A labor organization shall be, for purposes of this section, the authorized representative of those

persons receiving any retiree benefits covered by any collective bargaining agreement to which that labor organization is signatory, unless (A) such labor organization elects not to serve as the authorized representative of such persons, or (B) the court, upon a motion by any party in interest, after notice and hearing, determines that different representation of such persons is appropriate.

(2) In cases where the labor organization referred to in paragraph (1) elects not to serve as the authorized representative of those persons receiving any retiree benefits covered by any collective bargaining agreement to which that labor organization is signatory, or in cases where the court, pursuant to paragraph (1) finds different representation of such persons appropriate, the court, upon a motion by any party in interest, and after notice and a hearing, shall appoint a committee of retired employees if the debtor seeks to modify or not pay the retiree benefits or if the court otherwise determines that it is appropriate, from among such persons, to serve as the authorized representative of such persons under this section.

(d) The court, upon a motion by any party in interest, and after notice and a hearing, shall appoint a committee of retired employees if the debtor seeks to modify or not pay the retiree benefits or if the court otherwise determines that it is appropriate, to serve as the authorized representative, under this section, of those persons receiving any retiree benefits not covered by a collective bargaining agreement.

Appendix A

(e)

(1) Notwithstanding any other provision of this title, the debtor in possession, or the trustee if one has been appointed under the provisions of this chapter (hereinafter in this section "trustee" shall include a debtor in possession), shall timely pay and shall not modify any retiree benefits, except that —

(A) the court, on motion of the trustee or authorized representative, and after notice and a hearing, may order modification of such payments, pursuant to the provisions of subsections (g) and (h) of this section, or

(B) the trustee and the authorized representative of the recipients of those benefits may agree to modification of such payments, after which such benefits as modified shall continue to be paid by the trustee.

(2) Any payment for retiree benefits required to be made before a plan confirmed under section *1129* of this title is effective has the status of an allowed administrative expense as provided in section *503* of this title.

Appendix A

(f)

(1) Subsequent to filing a petition and prior to filing an application seeking modification of the retiree benefits, the trustee shall —

(A) make a proposal to the authorized representative of the retirees, based on the most complete and reliable information available at the time of such proposal, which provides for those necessary modifications in the retiree benefits that are necessary to permit the reorganization of the debtor and assures that all creditors, the debtor and all of the affected parties are treated fairly and equitably; and

(B) provide, subject to subsection (k)(3), the representative of the retirees with such relevant information as is necessary to evaluate the proposal.

(2) During the period beginning on the date of the making of a proposal provided for in paragraph (1), and ending on the date of the hearing provided for in subsection (k)(1), the trustee shall meet, at reasonable times, with the authorized representative to confer in good faith in attempting to reach mutually satisfactory modifications of such retiree benefits.

Appendix A

(g) The court shall enter an order providing for modification in the payment of retiree benefits if the court finds that —

(1) the trustee has, prior to the hearing, made a proposal that fulfills the requirements of subsection (f);

(2) the authorized representative of the retirees has refused to accept such proposal without good cause; and

(3) such modification is necessary to permit the reorganization of the debtor and assures that all creditors, the debtor, and all of the affected parties are treated fairly and equitably, and is clearly favored by the balance of the equities; except that in no case shall the court enter an order providing for such modification which provides for a modification to a level lower than that proposed by the trustee in the proposal found by the court to have complied with the requirements of this subsection and subsection (f): Provided, however, That at any time after an order is entered providing for modification in the payment of retiree benefits, or at any time after an agreement modifying such benefits is made between the trustee and the authorized representative of the recipients of such benefits, the authorized representative may apply to the court for an order increasing those benefits which order shall be granted if the increase in retiree benefits sought is consistent with the standard set forth in paragraph (3): Provided

further, That neither the trustee nor the authorized representative is precluded from making more than one motion for a modification order governed by this subsection.

(h)

(1) Prior to a court issuing a final order under subsection (g) of this section, if essential to the continuation of the debtor's business, or in order to avoid irreparable damage to the estate, the court, after notice and a hearing, may authorize the trustee to implement interim modifications in retiree benefits.

(2) Any hearing under this subsection shall be scheduled in accordance with the needs of the trustee.

(3) The implementation of such interim changes does not render the motion for modification moot.

(i) No retiree benefits paid between the filing of the petition and the time a plan confirmed under section *1129* of this title becomes effective shall be deducted or offset from the amounts allowed as claims for any benefits which remain unpaid, or from the amounts to be paid under the plan with respect to such claims for unpaid benefits, whether such claims for unpaid benefits are based upon or arise from a right to future unpaid benefits or from any benefits not paid as a result of modifications allowed pursuant to this section.

(j) No claim for retiree benefits shall be limited by section *502*(b)(7) of this title.

Appendix A

(k)

(1) Upon the filing of an application for modifying retiree benefits, the court shall schedule a hearing to be held not later than fourteen days after the date of the filing of such application. All interested parties may appear and be heard at such hearing. Adequate notice shall be provided to such parties at least ten days before the date of such hearing. The court may extend the time for the commencement of such hearing for a period not exceeding seven days where the circumstances of the case, and the interests of justice require such extension, or for additional periods of time to which the trustee and the authorized representative agree.

(2) The court shall rule on such application for modification within ninety days after the date of the commencement of the hearing. In the interests of justice, the court may extend such time for ruling for such additional period as the trustee and the authorized representative may agree to. If the court does not rule on such application within ninety days after the date of the commencement of the hearing, or within such additional time as the trustee and the authorized representative may agree to, the trustee may implement the proposed modifications pending the ruling of the court on such application.

(3) The court may enter such protective orders, consistent with the need of the authorized

representative of the retirees to evaluate the trustee's proposal and the application for modification, as may be necessary to prevent disclosure of information provided to such representative where such disclosure could compromise the position of the debtor with respect to its competitors in the industry in which it is engaged.

(l) This section shall not apply to any retiree, or the spouse or dependents of such retiree, if such retiree's gross income for the twelve months preceding the filing of the bankruptcy petition equals or exceeds $250,000, unless such retiree can demonstrate to the satisfaction of the court that he is unable to obtain health, medical, life, and disability coverage for himself, his spouse, and his dependents who would otherwise be covered by the employer's insurance plan, comparable to the coverage provided by the employer on the day before the filing of a petition under this title.

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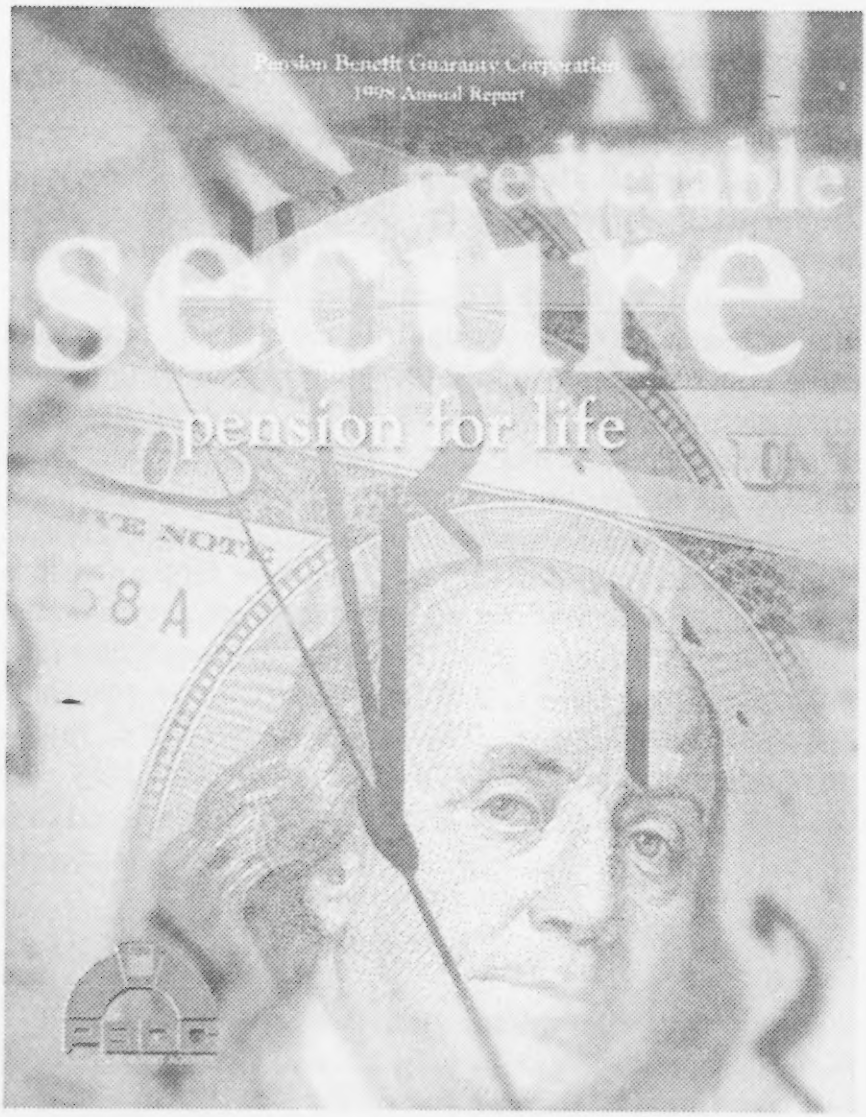
APPENDIX B — EXCERPTS FROM PBGC 1998 ANNUAL REPORT



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[Excerpt from page 14]

LOSS PREVENTION

Under its Early Warning Program, PBGC continued to monitor more than 500 companies with pension plans underfunded by at least $5 million in order to identify transactions that could jeopardize pensions and to arrange suitable protections for those pensions and the pension insurance program. During 1998, PBGC negotiators reached agreements valued at nearly $1.1 billion with 35 companies, including Pepsico, Fruit of the Loom, Sunbeam, Pillowtex, and Inland Steel Company. These agreements provided contributions, security, and other protections for the pensions of about 257,000 workers and retirees. Loss prevention is PBGC's principal performance measure for its strategic goal of protecting existing defined benefit plans and their participants; with regard to these agreements, PBGC is able to report a loss prevention rate of 100 percent for 1998.

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Appendix B

[Excerpts from page 23]

Financial Statements

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

General

The following discussion and analysis provide information that management believes is relevant to an assessment and understanding of the Corporation's financial condition and results of operations. The discussion should be read in conjunction with the financial statements and notes thereto.

PBGC's operating results are subject to significant fluctuation from year to year depending on the frequency and severity of losses from terminating pension plans, general economic conditions, and other factors such as changes in law. Consequently, certain traditional financial ratios and measurements are not meaningful and therefore, not presented.

Combined Results

For 1998, PBGC's combined underwriting and financial activities resulted in a net gain of $1.653 billion on gross income of $3.250 billion. The single-employer and multiemployer programs reported a net income of $1.531 billion and $122 million respectively. By law, these two programs are separate.

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SINGLE-EMPLOYER PROGRAM

Results of Activities and Trends: The net income in 1998 was $1.531 billion compared to net income of $2.612 billion in 1997. The $1.081 billion decrease was primarily attributable to the decrease in investment income.

Underwriting Activity: The gain of $462 million in 1998 was down from a gain of $897 million in 1997. This $435 million decrease was primarily due to (1) a decrease in premium income, (2) the one-time actuarial credit taken in 1997 as a result of the change in the method of calculating expenses incurred in determining and paying a participant's benefits, to more closely match the agency's annual claims-related expenses, and (3) an increase in losses from probable terminations.

Underwriting income decreased from $1.086 billion in 1997 to $976 million in 1998. The $110 million decrease relates primarily to the decrease in variable-rate premium payments.

The Corporation's losses from completed and probable plan terminations increased from $489 million in 1997 to $584 million in 1998. Although there were no major plan terminations in 1998, losses are unpredictable.

Operating costs remained level at $143 million.

Financial Activity: Investment income exceeded actuarial charges in 1998, resulting in a $1.069 billion gain versus a $1.715 billion gain in 1997. The total return on

investments was 14.4% in 1998, compared to 21.9% in 1997. Fixed-income investments experienced higher returns in 1998 than in 1997 while equity investment returns were lower. PBGC, in accordance with generally accepted accounting principles, marks its assets and liabilities to market.

Actuarial charges primarily resulted from the aging of the present value of future benefits and from changes in interest rates. In 1998, the select interest rate assumption decreased from 6.2% at September 30, 1997, to 5.7% at September 30, 1998, while the ultimate rate increased from 5.5% to 5.75%. The passage of time and change in the interest rates resulted in an actuarial charge of $1.034 billion in 1998, compared to an actuarial charge of $960 million in 1997.

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APPENDIX C — 58 FEDERAL REGISTER 50812 (SEPTEMBER 28, 1993)

PENSION BENEFIT GUARANTY CORPORATION

29 CFR Parts 2619 and 2676

RIN 1212-AA61

Valuation of Plan Benefits in Single-Employer Plans; Valuation of Plan Benefits and Plan Assets Following Mass Withdrawal

AGENCY: Pension Benefit Guaranty Corporation.

ACTION: Final rule.

SUMMARY: The Pension Benefit Guaranty Corporation ("PBGC") is amending its regulation governing valuation of plan benefits in terminated single-employer plans that are trusteed by the PBGC. The amendment revises the regulation's mortality assumptions to reflect recent acturial practice, (2) to uncouple the regulation's administrative expense ("loading") assumptions from its interest assumptions, and (3) to clarify the valuation of annuity benefits by prescribing a new interest rate structure that bases valuations on the length of time between the valuation date and the presumed date of each payment. Although the amendment continues the regulation's historical approach of assigning values to annuity benefits that are in line with private sector group annuity prices, and the PBGC anticipates that, for most plans, this amendment will not significantly affect the valuations produced, the new assumptions and structure will greatly enhance public understanding of the

PBGC's valuations. In addition, the PBGC is adopting unisex mortality assumptions when it is calculating de minimis lump sums (*i.e.*, those of $3,500 or less) to be paid to a participant; the PBGC is otherwise reserving the lump sum issue and therefore will otherwise continue to use its existing mortality assumptions and interest rate structure in the valuation of lump sum benefits.

At the same time, the PBGC is amending its regulation governing valuation of annuity benefits in multiemployer plans following mass withdrawal, so as to adopt the same mortality, loading, and interest assumptions as does the modified single-employer regulation. This change will result in simplification of calculations under the multiemployer regulation as well as greater consistency of annuity valuations between the two programs.

EFFECTIVE DATE: November 1, 1993.

FOR FURTHER INFORMATION CONTACT: Peter H. Gould, Senior Counsel, Office of the General Counsel, at the above address or at (202) 778-8850 ((202) 778-8859 for TTY and TDD). These are not toll-free numbers.

SUPPLEMENTARY INFORMATION:

Background

On January 19, 1993, the Pension Benefit Guaranty Corporation ("PBGC") issued a notice of proposed rulemaking (58 FR 5128) that would alter the structure and assumptions used in its valuation of annuity benefits. The

proposed rule would revise the PBGC's methods of valuing annuity benefits by adopting (1) a new table of mortality assumptions to reflect recent actuarial practice, (2) an administrative expense ("loading") assumption to replace the previous adjustment in the interest assumption that simulated this charge, and (3) a new structure of interest assumptions that is based on the period of time between the valuation date of a benefit and the presumed date of each payment of the benefit. The PBGC proposed these changes because, although the PBGC's existing assumptions and structure accurately reflect private sector group annuity prices, the disparity between the PBGC's low interest rates and familiar private sector rates had resulted in public confusion. The new annuity valuation structure and assumptions would make the annuity valuation process clearer to the public, and would more clearly conform to the current practices of the private insurance industry in pricing of group annuity benefits. The proposed rule would also adopt unisex mortality assumptions for lump sum valuations; this change would conform the PBGC's practice to that of private sector pension plans. Finally, the proposed rule would apply to valuations under terminated multiemployer plans under 29 CFR part 2676 as well as under terminated single-employer plans under 29 CFR part 2619.

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